

COMPANIES MENTIONED

Fastenal
FAST - \$42.20 - Hold**W.W. Grainger**
GWW - \$192.08 - Buy**MSC Industrial Direct**
MSM - \$71.04 - Hold**BB&TCM's Fastener Distributor Index (FDI) - Rough November, But Stable Outlook****KEY TAKEAWAY**

November's FDI weakened a bit in November, but in substance again idled just below the key 50 level. Notably, while November worsened, respondent's outlooks were no worse than stable and may have even improved a bit. We take this to mean the current period is being hurt by destocking and shutdowns but that these are viewed, rightly or wrongly, as having short shelf lives. It would seem to fit the narrative of a lull followed by reacceleration in 2013. The most worrisome element of the report was pricing, which is looking still softer.

KEY POINTS

About the Fastener Distributor Index (FDI). The FDI is a monthly survey of NorAm fastener distributors, conducted with the **FCH Sourcing Network**, which offers insights into current trends/outlooks. As a diffusion index, figures above 50 signal strength and below 50 signal weakness. It should be directly relevant to Fastenal and broadly relevant to other distributors (W.W. Grainger, MSC Industrial).

November was poor (46.1, vs. 46.8 in Oct.), but does not hinder the outlook. The erosion was not large, and in substance it probably doesn't materially alter the tone of what has been a very sluggish environment. In this reading, one metric stood out in particular: **Sales**. At 34.4 in November, it fell from 48.6 in October and registered the second worst reading this year. It is hard to say what blend of factors drove this: destocking, lengthy plant shutdowns, fallout from Hurricane Sandy, etc. *But it is pretty clear that November was tougher than October.*

But, perhaps tellingly, the 6-month outlook did not follow the FDI lower. November saw respondents take a stand about their six month outlooks. Happily, 47% of respondents anticipated higher activity six months out (34% in October). Unhappily, the pessimists also rose to 25% of total (25% in October). We take it as a positive the ratio of optimists and pessimists remained favorable despite a weak November and in the wake of the Presidential election. *This fits the narrative of an economy in a lull before firming up a bit in 2013.*

Pricing was the troubling metric. Pricing has gradually moderated throughout 2012. Sequential pricing was a bit softer (second time in three months) while annual pricing eased to its smallest gain of the year. *Indeed, we now consider year-to-year price to be basically "flattish" and something warranting close tracking.*

Supplemental query: would cancelling LIFO matter? Fiscal cliff negotiations have put eliminating LIFO back on the table. This could generate a large tax bill as LIFO reserves move to the P&L, and we were curious how that would be viewed by distributors. ~70% of respondents used FIFO and would not be affected. 16% saw it as a hassle but unlikely to alter their behavior. *We have been surprised at the lack of industry consolidation, and thought such a change may catalyze more of that. It seems there is less urgency than we would have expected.*

What does this mean for the "Big 3" distributors? These readings raise worries that November will pile on what was a weak October reading. Some of these trends may be mitigated at Grainger by its likely involvement in clean-up/recovery after Hurricane Sandy. But for the purer production names, Fastenal and MSC Industrial, this data suggests the set up to a poor Q4'12 continues. The silver lining is that this has not been unexpected and the outlook statement suggests the problem lies not with baseline demand but with transitory issues that should fade as we enter 2013. Time will tell.

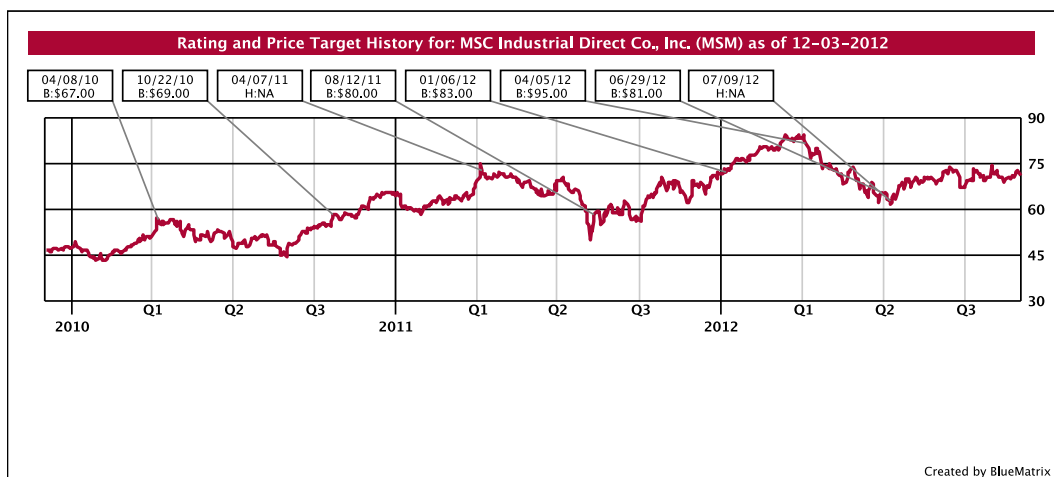
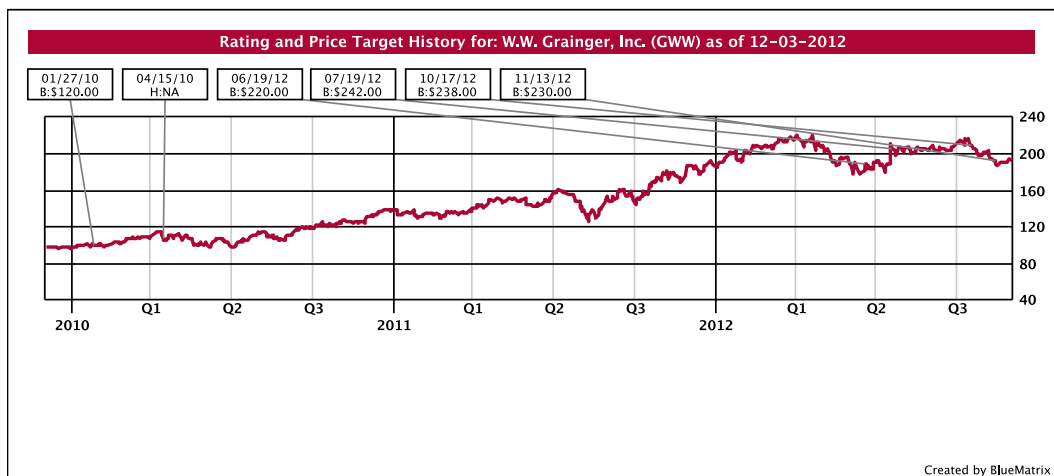
FASTENER DISTRIBUTION AT A GLANCE								
November 2012								
	Index - Nov.	Index - Oct.	Index - Sept.	Index - August	Index - July	Index - June	Oct.-->Nov. Change	Direction
PMI (Overall mfring sector)	49.5	51.7	51.5	49.6	49.8	49.7	0.2	Declining
FDI (Fastener distribution)	46.1	46.8	48.2	51.0	45.1	51.6	(1.4)	Declining
Sales	34.4	48.6	45.7	51.4	38.2	42.2	2.9	Declining
Employment	50.0	51.4	51.4	54.2	50.0	54.7	0.0	Declining
Supplier Deliveries	56.3	48.6	50.0	52.8	51.3	60.9	(1.4)	Slowing
Respondent Inventories	59.4	62.9	62.9	62.5	57.9	60.9	0.0	Too High
Customer Inventories	43.8	38.6	45.7	45.8	40.8	48.4	(7.1)	Too Low
Pricing, month-to-month	48.4	50.0	47.1	52.8	55.3	57.8	2.9	Lower
Pricing, year-to-year	53.1	58.6	55.7	66.7	61.8	56.3	2.9	Higher
	<u>Higher</u>	<u>Same</u>	<u>Lower</u>					
6-Month Outlook - Nov.	47%	28%	25%					

Sources: BB&T Capital Markets, FCH Sourcing Network, Institute for Supply Management

FDI and Pricing are diffusion indexes. At 50, the performance of the category listed met expectations. A reading above 50 suggests the category outperformed expectations, while a reading below 50 suggests the category underperformed expectations.

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Price Chart



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Not Rated (NR)	0.00%	Not Rated (NR)	0.00%

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